

**Nassau County Comptroller's  
Audit Advisory Committee  
2004 Annual Report**

## **Table of Contents**

	<b>Page</b>
<b>Executive Summary</b>	<b>2</b>
<b>Background and Purpose</b>	<b>4</b>
<b>Committee Composition</b>	<b>5</b>
<b>The Year in Review</b>	<b>6</b>
<b>Conclusion</b>	<b>11</b>
<b>Exhibit I – Audit Committee’s Mission Statement</b>	<b>12</b>
<b>Exhibit II – Economic Development Vertical Sub-Committee Report</b>	<b>13</b>
<b>Exhibit III – Financial Controls Sub-Committee Report</b>	<b>16</b>
<b>Exhibit IV – Nassau Healthcare Corporation Sub-Committee Report</b>	<b>19</b>

## **Executive Summary:**

**The Nassau County Comptroller's Audit Advisory Committee was established by the Comptroller in 2003 to provide outside advice and oversight for the county's financial and auditing operations. Of the Committee's seven members, two are government officials and five are county residents experienced in financial matters.**

During this first year of the Committee's operation, its members have reviewed the structure and finances of the County government, the outside auditing process, and have focused on matters of particular immediate concern, such as the fiscal health of the Nassau Health Care Corporation. The Committee has reviewed past and present audit reports, monitored the selection of the County's outside auditors, and reviewed the Comptroller's Office Field Audit Unit's 2005 internal audit plan. The Committee also examined the County's real estate tax refund process and the adoption of new Government Accounting Standards Board pronouncements ("GASB") of interest to the Committee.

The Committee established certain Sub-Committees to focus on issues of particular financial concern. Three Sub-Committees were formed (the Sub-Committee reports are attached as Exhibits):

THE ECONOMIC DEVELOPMENT VERTICAL ("EDV") SUB-COMMITTEE was charged with reviewing the financial mismanagement uncovered at the EDV; whether these problems were systemic in the County, and the actions taken by the administration to rectify them. The Committee concluded that the County is moving to establish a good overall internal control environment with related accounting policies and procedures. The Sub-Committee recommends that the initiatives the County has undertaken to document accounting procedures and internal controls be given a high priority; that all quasi-governmental organizations within the County be contractually obligated to establish sound accounting procedures and internal controls; and that the administration continue its efforts to increase the number of professional managers and institutionalize requirements wherever possible.

THE FINANCIAL CONTROLS SYSTEM SUB-COMMITTEE was formed to gain a better understanding of the County's financial controls system ("FCS"), particularly as it relates to expenditures. While the FCS appears adequate, the Sub-Committee concluded that the administration should continue with its documentation initiatives on a high priority basis; identify critical points of analysis during the documentation and enhance procedures; compensate for employee turnover by institutionalizing procedures where possible; and perform audits of departmental review and approval procedures.

THE NASSAU HEALTHCARE CORPORATION ("NHCC") SUB-COMMITTEE was charged with reviewing the financial problems facing NHCC; the financial impact of NHCC's fiscal crisis on the County; and the steps NHCC has taken to improve its overall financial situation. In summary, the Sub-Committee concluded, based upon discussions with the County's Medical Center consultant, NHCC management, the County Attorney and the Comptroller, that the

situation at NHCC appears to be somewhat improving as a result of measures such as staff reductions and debt refinancing but the situation remains quite difficult. Additional recommendations to ameliorate NHCC's financial condition are being considered by the Corporation. In short, the situation at NHCC continues to warrant careful monitoring and the Sub-Committee will continue to request status updates.

The Committee is also continuing to review:

- The County's tax certiorari refund process, its progress in reducing the backlog of old claims and, accordingly, its tax certiorari liability, and its progress in streamlining the process.
- Corrective actions underway within the Treasurer's Office to improve processing controls.
- The treatment of pension payments in budgetary and financial statements following current discussions between the State Comptroller and the Government Accounting Standards Board
- Audit reports and corrective action plans concerning County operations.

## **Background and Purpose:**

The Nassau County Comptroller's Audit Advisory Committee ("Committee") was established to assist in the monitoring of Nassau County's finances, its financial statements and the review of those financial statements by the County's outside auditors. In addition, the Committee advises the Comptroller concerning audits performed by his Office.

The Committee assists in monitoring the independent audit of the County's financial statements from the selection of the independent auditor to providing advice on the resolution of audit findings. The Committee examines the appropriateness of the outside audit's scope; the preparation of the annual financial statements; the audit results; and the assessment of the adequacy of internal controls by both the administration and the auditors. Similarly, the Committee will review and comment on the Comptroller's internal audit plan, audits prepared pursuant to that plan, agency responses, and County control directives and procedures. Additionally, when appropriate, the Committee will periodically participate in special projects.

## Committee Composition:

The Committee is composed of seven members:

- County Executive or designee
- County Comptroller or designee
- Five experienced County community/business/financial leaders selected by the Comptroller who are independent of the County and local governments. One of the five non-County members is chosen to serve as committee chairperson.

Current members of the Committee are:

**H. Richard Grafer:** A retired Partner and Managing Director of Arthur Andersen LLP, is sole owner and Managing Member of Pathway Investments, LLC, a venture capital firm investing in companies with a social mission.

**Manuel Mosquera:** Nassau County's Deputy Comptroller for Audits and Special Projects (serving as designee of the County Comptroller).

**Ralph S. Polimeni:** Dean of the Frank G. Zarb School of Business at Hofstra University, where he also holds the Chaykin Endowed Chair in Accounting. Mr. Polimeni is currently the Chairperson of the Committee.

**Edward S. Scott:** Deputy General Counsel and Vice President of Development and Acquisitions for UrbanAmerica, LP.

**Terence E. Smolev:** Partner in charge of tax, trusts and estates with the law firm of Forchelli, Curto, Schwartz, Mineo, Carlino & Cohn, LLP. Mr. Smolev is currently the Vice Chairperson of the Committee.

**Robert Andrew Wild:** Chairman and Managing Partner of Garfunkel, Wild & Travis, P.C., a law firm specializing in healthcare.

**Martha Herrera-Wong:** Deputy Budget Director in the Nassau County Office of Management and Budget (serving as designee of the County Executive).

In addition, the County Comptroller and a partner of Deloitte & Touche, the County's current outside audit firm, attend every Committee meeting.

Service on the committee is pro-bono. County officials serving on the committee will not receive compensation in addition to their regular salaries. Outside members of the Committee serve staggered terms so as to ensure continuity and stability.

## **The Year In Review:**

The first Committee meeting took place on October 7, 2003. It served as an introductory session for the various Committee members as well as an opportunity for the County Executive and the County Comptroller to officially welcome the members. The County Executive and Comptroller presented an overview of the County's organizational structure, a brief history of the County's fiscal crisis, and a description of the current state of the County's financial situation. Representatives of Deloitte and Touche were also present and commented on the County's financial progress.

In subsequent meetings, the Committee addressed numerous issues. After addressing operational issues, including the adoption of a Committee mission statement (see Exhibit I) and member terms, the Committee focused on reviewing County financial issues and the County's previous five years of audited financial statements and management letters.

The Committee noted repeated findings in earlier audited financial reports concerning serious lapses of internal controls and uncertain financial outlook and the failure of the previous administration to address these findings, resulting in the County having received "qualified" auditor's opinions,

In view of this background, the Committee was pleased to note that the outside auditors had given the County's 2002 financial statements an "unqualified" opinion. While some internal control issues remained, the Committee members and the outside auditor noted that the County appeared to be in the process of addressing them.

Soon after the Committee's inaugural meeting, the County's Economic Development Vertical (EDV) came under intense public scrutiny. Concurrently, the fiscal crisis at the Nassau Health Care Corporation (NHCC), a public benefit corporation that operates the Nassau University Medical Center and the A. Holly Patterson nursing home, and its potential adverse impact on the County's finances, were of growing concern. In view of the large amount of material that the Committee was reviewing, and the complexity of the issues involved, the Committee decided to meet every other month, rather than quarterly, as originally planned.

The Committee has established a number of sub-committees:

- A. **ECONOMIC DEVELOPMENT VERTICAL SUB-COMMITTEE** (Richard Grafer, Manuel Mosquera and Martha Wong): reviewed financial control issues and corrective measures taken in the Economic Development Vertical. The Sub-Committee's report is attached as exhibit II, listed below are some of the highlights:
  - Policies and procedures that have evolved over the years have been largely unwritten and passed-down from administration to administration, mostly by word of mouth. It appears that this lack of formal documentation coupled with the independent status of several entities within the EDV were major contributing factors to the problems that befell the EDV. As a result, a Chief Compliance Officer has been nominated to oversee an initiative to establish formal, sound accounting policies and procedures;

additionally, the Comptroller's office will continue to issue broad internal control directives with county-wide applicability.

- Many of the above initiatives undertaken will be "institutionalized" or "codified" via legislative action (such as multi-year budgeting requirement) so as to ensure such improvements continue in future administrations.
- To the degree that there are any other quasi-governmental entities within the County, they should be placed under the County's financial control system or subject to a contractual relationship with the County.

The overall conclusion was that the County is moving in the right direction to establish a good overall internal control environment with related accounting policies and procedures. The Sub-Committee recommends that the administration continue its efforts to increase the number of professional managers and institutionalize requirements wherever possible.

B. COUNTY FINANCIAL SYSTEM AND PROCESSES SUB-COMMITTEE (Richard Grafer, Manuel Mosquera and Martha Wong): as a follow-up to the Comptrollers review of internal controls in the Economic Development Vertical, this Sub-Committee was formed to familiarize itself with accounting procedures and internal controls throughout the County. A particular emphasis was placed on processes concerning expenditure approval and payment. The Sub-Committee's report is attached as exhibit III, listed below are some of the highlights:

- Documentation of County policies and procedures needs improvement. As noted in the above section, several initiatives are underway to correct this problem. The Sub-Committee suggested that it monitor progress in this area.
- It is not clear whether enough high level analysis is performed at critical points in the processing cycle; however, it is logical to assume that the documentation initiatives will address these shortcomings.
- Employee turnover, particularly with respect to key personnel, could negatively impact the FCS. While management succession planning may not be feasible within a government setting, attempts to institutionalize as many procedures as possible will help to minimize this shortcoming.
- The administration has noted that it is committed to addressing the delinquency in the preparation of monthly bank reconciliations. Additional research and investigation is required with respect to the processing of manual checks, wire transfers, debt service payments and any other payments that do not go through the FCS process. Sub-Committee suggested that it continue to monitor this area.
- The manner in which some departments determine the authorized signatory, for claims processing, and the specific procedures to be followed are often left to the discretion of the department. Thus there could be undetected weaknesses in these procedures at the departmental level.

The Sub-Committee's conclusions are that, the administration continue with its documentation initiative; identify critical points of analysis during the documentation stage and enhance procedures; compensate for employee turnover by institutionalizing procedures where possible; audits be performed of departmental review and approval procedures.



- C. NHCC SUB-COMMITTEE (Terence Smolev and Robert Wild): reviewed the financial condition of NHCC and the impact on the County should NHCC be unable to meet its financial obligations. Additionally, it reviewed the NHCC report completed by Manatt, Phelps & Phillips for the county, and NHCC's actions in response to that report. The Sub-Committee also discussed these issues with the newly appointed interim CEO of NHCC. The Sub-Committee's report is attached as exhibit IV, listed below are some of the highlights:
- Summary presentation of the County's consultant report on NHCC, outlining its current status as well as listing various recommendations.
  - Update on a Stabilization Agreement entered into between the County and NHCC, providing resolution of various "due to/from" obligations, which benefited NHCC but had no negative impact on the County. Additionally, audit powers over NHCC were granted to the County Comptroller.
  - Presentation of NHCC's bond refinancing plan, which subsequently took place and is expected to save NHCC approximately \$28 million over the life of the debt.
  - Issues regarding the A. Holly Patterson Nursing Home were discussed and the Sub-Committee advised that the intent is to diminish the size of the nursing home, relocate it and sell off the excess beds, subject to regulatory approval.

In summary, based upon discussions with the County's consultant, NHCC management, the County Attorney and the Comptroller, the situation at NHCC appears to be somewhat improved. While it is too early to note to what extent the consultant's recommendations may result in financial relief to NHCC (other than the layoffs and bond refinancing that have already taken place), it appears that various recommendations are being actively researched. In short, the situation at NHCC continues to warrant careful monitoring and the Sub-Committee will continue to request status updates.

- D. REPORT SUB-COMMITTEE (Ralph Polimeni, Robert Wild and Manuel Mosquera): drafts Audit Committee reports (such as the Interim Report the Committee previously issued and this report).

In addition to the focus on specific issues by the sub-committees, the Committee, as a whole, was briefed on other County financial matters. At the beginning of each meeting, Comptroller Weitzman provided the Committee with an update on major financial or operational issues facing the County. For example:

#### TAX CERTIORARI

Comptroller Weitzman discussed the County's tax certiorari refund process and its impact on the County's finances. The Comptroller noted that clearing the tax certiorari backlog is one of the biggest financial hurdles facing the County. The tax certiorari issue is particularly important as the County shifts from issuing debt to pay for refunds to paying them out of operating funds on a go-forward basis.

#### PENSION PAYMENTS & OTHER ACCOUNTING ISSUES

Comptroller Weitzman informed the committee of a current pension payment accounting treatment issue arising from newly enacted legislation deferring the pension payment due date

and allowing for the establishment of pension reserves. He noted that the State Comptroller and the Government Accounting Standards Board (GASB) are in discussions on the treatment of pension payments between budgetary and financial statements. It is expected that the likely outcome will be that financial statements will be in accordance with generally accepted accounting principles (GAAP) and show the accrual for the pension payment for the year ended 2004 and that the County's budgetary statements will report the pension payment in February of 2005, when made. The Administration has indicated they expect to use this budgetary savings of approximately \$80 million dollars to establish pension reserves to offset the large pension increases expected in future years. This treatment is in accordance with the intent of the new legislation.

Deputy Comptroller Randy Ghisone noted that GASB 45, Financial Reporting for Post Employment Benefit Plans Other Than Pensions, scheduled for implementation for the year ending 2007, will require the County to "recognize" the liability related to such retiree benefits. While this pronouncement will not have a direct impact on the County's budget, it is estimated that the recognition of these obligations will add a liability of approximately \$2 billion dollars to the County's full accrual balance sheet.

#### AUDITING FIRM ENGAGEMENT

Randy Ghisone, the County's Deputy Comptroller for Accounting, outlined for the Committee the major points of the 2003 Comprehensive Annual Financial Report (CAFR), and the Committee was briefed on the County's RFP process to solicit proposals for an outside accounting firm to complete the County's annual audit, which was personally monitored by the Committee Chairperson. The accounting firm of Deloitte and Touche was awarded the contract.

#### INTERNAL AUDIT PLAN

Deputy Comptroller of Audits, Manuel Mosquera, presented the Committee with copies of the 2004 Internal Audit Plan, as well as the preliminary 2005 Internal Audit Plan. He described the auditee selection process, which includes factors such as the size of the department's budget or revenue generation, date of last audit, whether certain department units are of particular concern, and a risk assessment (including an analysis of whether there have been significant changes in the department that effect the need for audit review, such as changes in procedures, introduction of new systems, changes in personnel, etc.).

#### EXTERNAL AUDIT PLAN

Robert Rooney the Deloitte & Touche partner in charge of the County's outside audit, presented the Committee with an overview of Deloitte's 2004 audit plan, including the engagement team, the audit scope (covering both the planning and testing/evaluation phases) as well as a discussion of upcoming Government Accounting Standards Board ("GASB") pronouncements (and their applicability, if any, to the County).

#### MANAGEMENT LETTER

Additionally, Mr. Rooney reviewed the 2003 Management Letter comments. He noted that the number of management letter comments has decreased under the current administration, but that there are still issues that need to be addressed. One area of concern continues to be Treasurer's Office operations. Because of these concerns, the Committee met with Deputy County Executive

Arthur Gianelli and Treasurer Henry Dachowitz for briefings on corrective actions being taken in the Treasurer's Office. According to Deputy County Executive Gianelli, the turnaround of the Treasurer's Office is a priority for the County administration. He and the County Treasurer will update the Committee at its January meeting.

#### SUCCESSION PLANNING

Another issue of concern to the Committee is the lack of a formal succession plan for middle to senior management, and, in particular, non-union management. Succession planning in a governmental setting is more difficult than in the private sector because in government, elected officials, who do not remain in office indefinitely, have appointment power over non-civil service management.

#### SUMMARY

As previously mentioned, two matters that could seriously impact the finances of the County are the financial well being of NHCC and the funding of real estate tax refunds. The Committee was pleased to see significant improvement on both fronts. Comptroller Weitzman noted that a stabilization agreement between the County and NHCC had been signed. As a result of this agreement, all outstanding claims through the end of 2003 have been settled (previously, the calculation of items in dispute was as high as \$140 million). Additionally, the County Comptroller's office has now been granted audit authority at NHCC and the County has control over how NHCC will use the funds obtained from a refinancing agreement that significantly lowered existing county guaranteed NHCC debt. While the situation at NHCC is still of concern, definitive progress has been made by the Administration and the new management team at NHCC.

The second significant issue facing the County concerns the real estate tax refund process. Deputy County Executive Arthur Gianelli spoke to the Committee regarding the Administration's progress in reducing the tax certiorari liability by working on the backlog of old claims and attempting to streamline the current tax certiorari process. This issue is critical to the County; it must fund all tax certiorari refunds out of operating funds by December 31, 2005. The County continues to make processing of these claims a priority, as well as examining alternatives to further reduce them.

The Committee was pleased to note the progress the county has made in moving from a financial crisis to multiple credit rating upgrades within the last two years. Additionally, the Committee noted that certain initiatives implemented by the current Administration, such as the issuance of a multi-year plan, are being institutionalized in legislation, to insure these "best practices" continue going forward.

## **Conclusion:**

As Nassau County's Audit Advisory Committee completes its first year, it has become educated concerning County operations, the financial challenges facing the County, and the accomplishments the County has achieved during the past three years.

As part of the Comptroller's effort to make government "transparent", the Committee is made aware of all major financial issues facing the County. The Administration has given Committee members access to County employees and financial information. The Committee has acknowledged where improvements have been made, and has noted areas where more progress is necessary. During the coming year, the Committee intends to follow-up on issues already examined as well as to monitor new matters that may arise.

## **EXHIBIT I**

### **Mission Statement Nassau County Comptroller's Audit Advisory Committee**

The Nassau County Comptroller's Audit Advisory Committee was established to answer the call to assist in the monitoring of Nassau County's financial integrity. Its mission is to assist in the monitoring of the independent audit of the County's financial statements from the selection of the independent auditor to the resolution of audit findings. Specifically, the committee will assist in monitoring the following: selection of the outside, independent auditors; the appropriateness of the scope of the outside audit; the preparation of the annual financial statements; the results of the audit; and the assessment of the adequacy of internal controls by both the administration and the auditors. The Committee will have a similar responsibility to assist in monitoring the establishment of the internal audit plan and reviewing the results thereof. Periodically, it will participate in special projects; review special district audits filed annually with the Comptroller; and review audits of county agencies prepared by the Comptroller, agency responses to those reports, and county control directives and procedures. This committee will review the process that exists for providing that the county's financial statements and audits are in compliance with the pronouncements of the Government Auditing Standards Board ("GASB"). It is committed to upholding continued excellence in Nassau County Government.

## **EXHIBIT II**

**TO:** THE NASSAU COUNTY ACCOUNTING AND AUDIT ADVISORY COMMITTEE

**FROM:** THE SUB-COMMITTEE ON THE ECONOMIC DEVELOPMENT VERTICAL (“EDV”) AND RELATED INTERNAL CONTROL ISSUES (MEMBERS: H. RICHARD GRAFER, CHAIRMAN, MANUEL MOSQUERA AND MARTHA WONG)

**SUBJECT:** SUMMARY OF THE SUBCOMMITTEE’S FINDINGS

**DATE:** MAY 8, 2004

### **INTRODUCTION**

The sub-committee met with various county officials in order to accomplish the following:

1. Discuss and understand the much-publicized problems occurring recently at the EDV.
2. Determine on a high level basis whether or not there are any broader implications resulting from such problems, particularly as they relate to the county’s overall internal control environment.
3. Determine what actions have been taken to date by the county to rectify such problems and deal with any broader implications.

In conducting its review, the sub-committee developed and used a questionnaire and reviewed certain other information made available to it. However, the review was by no means detailed, and it involved no testing or other means of verification. Discussion and inquiry were the primary means of review used.

### **FINDINGS**

1. **Problems Identified And Actions Taken By The County**--- After the problems at the EDV were first identified, the Comptroller’s Office performed an audit of certain functions and activities within the EDV and issued a corrective action plan (“CAP”) as a result. A county “reform” committee was established to respond to the CAP and has been working diligently to eliminate the problems identified. A detailed response to the CAP will be issued in the near future although many of the CAP recommendations have already been implemented.

While it’s dangerous to generalize about the cause of the problems at EDV, particularly since there were many, it appears that their independent corporation status of several entities within the EDV and the fact that there was no initiative to establish basic policies and procedures (operational as well as accounting) at the time the EDV was formed were major contributing factors.

In addition, the county has never had a countywide accounting policies and procedures manual. Nor has it had any formal internal control guidelines that individual departments could follow in establishing their own accounting policies and procedures. The policies and procedures that have evolved as a result on a department-by-department basis have been largely unwritten and passed-down from administration to administration mostly by word of mouth. This has resulted in the inconsistent application of basic principles, particularly when downsizing or employee turnover have occurred and/or unique organizational structures, such as the EDV, have been put in place. The need for a better and more formalized internal control environment has been recognized for a while, but it didn't become a priority until the EDV problems surfaced.

The county has undertaken two initiatives to address the lack of formalized accounting policies and procedures. First, a Chief Compliance Officer was hired to oversee an initiative to establish formal, sound accounting policies and procedures. This initiative is underway, and its first step involves retaining outside accounting firms to work with individual departments to (a) "inventory" and evaluate existing accounting policies and procedures, (b) establish new, sound accounting policies and procedures, where appropriate and (c) formalize all such policies and procedures. (November 2004 Update: One firm has already been retained and has begun working in a high priority area, and a second firm is about to be retained). The second initiative is being undertaken by the Comptroller's Office to issue broad internal control directives that have application countywide. The goal at some point in the future is to link-up the first and second initiatives to ensure that each department's policies and procedures conform to basic principles of internal control. In addition, each department will be asked to establish a system of communicating these policies and procedures to its employees and educating new employees concerning them.

2. **Timetable**---This is obviously a long-term project, which could extend over the course of several administrations. Because of its critical importance, there needs to be some mechanism to ensure that the project does not die under a new administration. The risk of this happening can be reduced in the following fashion:
  - a. First, the present administration is attempting to hire more professional managers regardless of political affiliation. Such managers will not only bring a greater level of expertise and competence to the job, but they will also be more likely to survive a change in administration.
  - b. Secondly, the results of the initiatives undertaken will be institutionalized" or "codified" within the county charter and/or via legislative action wherever and whenever possible so that future administrations will be required to adhere to sound accounting policies and internal control procedures. This has already been done with respect to the NIFA multi-year budgeting requirement, and the administration is in the process of establishing similar policies with respect to debt and investments. The Chief Compliance Officer also plans to establish milestones and timetables to ensure that the process does not get delayed.

- 3. Other Accounting And Control Implications**---The EDV is quite unique in its structure and is not exactly replicated in other parts of the county's operations. However, the parks department does have some quasi-governmental entities within it (Nassau Heritage, Nassau First and the Aviation and Space Museum), which need to be either brought under the county's financial control system or, at a minimum, subject to a contractual relationship with the county. In addition, certain specific areas of operation and expenditure may need some attention to ensure that they are better controlled.

## **CONCLUSIONS AND RECOMMENDATIONS**

It's apparent that the County is moving in the right direction to establish a good overall internal control environment and related sound accounting policies and procedures. It's important that this initiative maintain the high priority that it presently seems to have. Thus, we recommend that the sub-committee periodically meet with county officials to review progress.

As noted earlier, we are also concerned that this initiative might die with any change in administration, particularly in view of its long-term nature. This would be unfortunate and not in the best interests of county residents. Therefore, we strongly encourage the administration to continue its efforts to increase in the number of professional managers and "institutionalize" or "codify" requirements wherever possible.



### **EXHIBIT III**

**TO:** THE NASSAU COUNTY ACCOUNTING AND AUDIT ADVISORY COMMITTEE

**FROM:** THE SUB-COMMITTEE ON THE COUNTY FINANCIAL CONTROL SYSTEM (“FCS” A/K/A “NIFS” AND “THE FINANCIAL SYSTEM”) (MEMBERS: H. RICHARD GRAFER, CHAIRMAN, MANUAL MOSQUERA AND MARTHA WONG)

**SUBJECT:** SUMMARY OF THE SUB-COMMITTEE’S ACTIVITIES AND FINDINGS

**DATE:** NOVEMBER 25, 2004

#### **INTRODUCTION**

The sub-committee was formed to gain a better understanding of the county’s financial control system (“FCS”), particularly as it relates to expenditures. This system is the basic accounting and control system within the county, and much confidence is placed in it to prevent unauthorized expenditures and other irregularities. By gaining a better understanding of the system, the sub-committee hoped to determine on a very high-level basis whether or not this confidence is justified.

To develop its understanding of the system, the sub-committee met with various county officials, including the head of the county’s vendor claim department (“CVC”), which performs much of the processing of vendor claims (invoices) and is responsible for executing many of the control procedures with respect thereto. The sub-committee would have liked to review written accounting policies and procedures with respect to the FCS, but none exist in any formalized, comprehensive fashion (see “FINDINGS” below). Consequently, the sub-committee necessarily relied on its discussions and follow-up inquiries with county officials. No testing or other means of verification was used, so the findings submitted by the sub-committee should not be considered complete or certain.

#### **FINDINGS**

- 1.**        **General**---The policies and procedures employed by the county to process and control expenditure transactions appear good. However, certain improvements could be made, and certain areas could be investigated further as noted in the following paragraphs.
  
- 2.**        **Lack of Documentation**---As discussed in detail in another sub-committee report concerning the economic development vertical (EDV”), the county has never had a countywide accounting policies and procedures manual or formal internal control guidelines. Thus, documentation of the FCS to any great degree is lacking. However, as noted in the EDV sub-committee report, several initiatives are underway to correct this problem over a period of time

on a countywide and department-by-department basis. The committee should monitor progress made on these initiatives on a regular basis since the sub-committee considers them to be extremely important.

- 3. Analysis of Transactions**---It's not clear whether enough high level analysis is performed at critical points in the processing cycle. However, it is logical to assume that the documentation initiatives noted above will highlight such critical points, and appropriate review and analysis procedures can then be designed and implemented. In addition, the comptroller's audit staff examines approval paths during its operational audits, which should serve to highlight critical points in the specific departments and functions it audits while the broader documentation initiatives are being completed.
- 4. Lack of Succession Planning**---Employee turnover, particularly with respect to key personnel, could negatively affect the FCS in the future. No formal succession planning exists to address this issue, and, for that matter, it may not be possible to establish such planning within the environment the county operates and without legislative initiatives. However, as noted in the EDV sub-committee report, the administration is attempting to "institutionalize" and "codify" as many procedures as it can. This, plus the documentation initiatives noted above, will help alleviate the succession-planning problem somewhat, but this is probably a problem that can never be solved completely.
- 5. Bank Reconciliations**---The delinquency in the preparation of monthly bank reconciliations has been well documented in the independent auditors' management letter, and both the treasurer's department and the administration have advised us that they are committed to correcting this problem in the future. However, we believe that additional research and investigation is required with respect to the processing of manual checks, wire transfers, debt service payments and any other payments that don't go through complete FCS processing procedures. Such additional research and investigation may also be required with respect to cash receipts received directly by the treasurer's department. Finally, the bank reconciliation process may have to be modified to include review and approval by someone outside the treasurer's department if any weaknesses are detected in the above-mentioned areas. Some of this research and investigation has already begun. The committee and sub-committee should continue to explore and monitor this whole area, particularly once the delinquency problems have been addressed.
- 6. Departmental Review and Approval Procedures**---Individual departments are required to designate an "authorized person" to review and approve claims prior to submission to the CVC. The manner in which such departments determine the "authorized person" and the specific procedures they require the authorized person to follow in completing the review is left to the discretion of the department. Thus, there could be some undetected weaknesses in these procedures at the departmental level. Field audits focus on this subject to

some extent but not comprehensively. The sub-committee recommends that future annual audit plans include a few comprehensive audits of this area beginning with those departments that seem to have the greatest number of differences/exceptions arising during CVC processing. Consideration should also be given by the administration to including this area in the documentation initiatives noted earlier.

## **CONCLUSIONS AND RECOMMENDATIONS**

As noted in our first finding above, the county's FCS appears to be good. However, we have the following recommendations concerning improvements that could be made and/or additional investigation that may be necessary:

1. The administration should continue to aggressively pursue the documentation initiatives begun in 2004, and the committee should monitor progress on a regular basis.
2. The administration and the comptroller's office should strive to identify critical points of analysis during the documentation initiatives and field audits and enhance procedures where appropriate.
3. The administration should compensate for turnover in key employees to the extent possible by identifying the resulting risk, "codifying" procedures wherever possible and enhancing procedures when codification is not possible.
4. The administration, committee and sub-committee should continue to monitor progress in the bank reconciliation area and explore the other areas noted above that could contain additional weaknesses.
5. Future comprehensive audits should be performed of departmental review and approval procedures, particularly of those departments having the greatest number of differences/exceptions arising during CVC processing.

**EXHIBIT IV**  
**FINAL REPORT**  
**NASSAU COUNTY AUDIT COMMITTEE**  
**REVIEW OF THE NASSAU UNIVERSITY MEDICAL CENTER**

**TO:** THE NASSAU COUNTY ACCOUNTING AND AUDIT ADVISORY  
COMMITTEE  
**FROM:** THE SUB-COMMITTEE ON THE NASSAU UNIVERSITY MEDICAL  
CENTER  
**SUBJECT:** SUMMARY OF THE SUBCOMMITTEE'S FINDINGS  
**DATE:** JANUARY 3, 2005

**INTRODUCTION**

The Subcommittee met with representatives of the County and of the Medical Center on two occasions to accomplish the following:

1. Discuss and understand the problems and proposed restructuring/remissioning of the Medical Center.
2. Determine the extent, if any, to which the current financial condition of the Medical Center would impose liability on the County beyond that which it has experienced from year to year (either legally or from a practical point of view).
3. Determine the extent to which the Medical Center has taken steps to improve its financial situation (particularly with respect to implementation of the recommendations of the consultant [described below]).

The methodology used by the Subcommittee to develop responses to the foregoing issues was to interview Medical Center administration, representatives of the consultant, the Comptroller, representatives of the County executive, representatives of the County attorney and to receive and review the consultant's report (dated January of 2004) and interim financial information. The review by the Subcommittee involved no testing or other means of verification. Discussion and inquiry were the primary means of review.

**FACTS AS PRESENTED TO THE SUBCOMMITTEE**

**Meeting of May 5, 2004**

The initial meeting regarding the Medical Center was held on May 5, 2004. In attendance were Terence Smolev, Manny Mosquera and Robert Wild as members of the Subcommittee, Art Gianelli, Arda Nazerian, Lorna Goodman, George Kalkines and Jeff Thrope (Mr. Kalkines and Mr. Thrope representing the consultant, Manatt Phillips) (the "Consultant").

### **The Following are Significant Facts Presented as of May 2004**

1. The Medical Staff was overstaffed and as of May 2004, the Medical Center had laid off approximately 400-500 workers.
2. The Medical Center was losing about \$1.5 million per month (described as on target with expectations).
3. The Consultant prepares monetary reports on a cash basis every month and works with Comptroller Weitzman so that the Medical Center's cash position is actually reviewed every two weeks.
4. The Consultant projected that the Medical Center would run out of cash precisely at the end of the year (this result is brought about in part by a delay in pension funding).
5. The overall plan of the Medical Center includes continued County funding of \$52-54 million per year (\$18 million in essentially direct subsidies and historic mission payments and the balance for direct services by the Medical Center to the County).
6. There was no anticipation of additional subsidy payments required and steps were being taken to implement the Consultant's report although apparently other than lay offs there had not been significant accomplishments as of that date. There were some "positive" appeals under the Medicare and Medicaid programs which could increase the financial position of the Medical Center.
7. The major undertaking which would have a positive financial effect had to do with refinancing of debt applicable to the Medical Center. As of this interview, the closing of the refinancing had not yet taken place.

### **Meeting of September 22, 2004**

On September 22, 2004 a second meeting was held at which Daniel Kane, the President and CEO of the Medical Center was present as was George Kalkines and Jeff Thrope of the Consultant.

The purpose of this meeting was to determine how the issues identified at the first meeting had been addressed to that point and what were the future plans to improve the financial conditions of the Medical Center.

The Subcommittee was advised as follows:

1. The Board of the Medical Center had adopted a resolution calling for the implementation of the recommendations of the Consultant.
2. The bond issue referred to at the May meeting was discussed (a closing was described as imminent). An agreement had been entered into between the County

and the Medical Center which will provide a benefit of approximately \$18.5 million to the Medical Center with no detriment to the County. The bond issue, as is currently the case, is to be (and now is) guaranteed by the County.

3. The expectation was that the bond issue would save the Medical Center approximately \$28 million over the life of the debt (virtually all of the benefit realizable in the first five years).
4. A Stabilization Agreement entered into between the County and the Medical Center provided for a resolution of a series of “due to and due from” obligations which also improved the Medical Center’s position and, as advised by the Comptroller, had no negative impact on the County (as the indebtedness from the Medical Center had been fully reserved years earlier).
5. The new bond issue parallels the current bond issue in that any default by the Medical Center which would trigger a guarantee by the County of the bonds would not require an acceleration of the indebtedness but rather would allow the County to pay off the bonds as if no default had taken place.
6. The Consultant and the Medical Center President believed that position of the County vis a vis the Medical Center has been improved by a new Regulatory Agreement which provides significant oversight by the County and at the same time provides for a mortgage on the Medical Center’s real estate (the new bond issue itself is not secured by such a mortgage – thus giving the County a first lien on the Medical Center property) (something which did not previously exist).
7. The report on the cash position as of September indicated that the “year end running out of cash prediction” was still on target. In fact the issuance of the bonds and the success of DOH appeals would (as reported) provide for about 18 months of cash although at this point, it was not clear as to what would happen if the new bond issue did not go forward.
8. Issues regarding the A. Holly Patterson Nursing Home were discussed and the Consultant advised that there is an intent to diminish the size of the nursing home, relocate it and sell off the excess beds, subject to regulatory approval. The proceeds of the sale will, to some extent, reduce the outstanding indebtedness.

<sup>1</sup> *We have been advised since the September meeting that the bond issue has gone forward.*

<sup>2</sup> *We have been advised that the process of selling off excess nursing home beds is underway.*

## **CONCLUSION**

### **IMPACT OF THE COUNTY/ADOPTION OF CONSULTANT RECOMMENDATIONS**

Based upon discussions with the Consultant, Medical Center representatives, the County attorney and the Comptroller, it appears that the “legal” exposure to the County for any failure of the Medical Center is no greater than it has been in the past and in fact, the situation appears to have been somewhat improved by the financial benefits derived from the new bond issue and by the fact that the County now holds a mortgage on the real property which it did not hold before.

It is not clear to us (and it should be pursued) as to the extent to which the Consultant’s recommendations other than the layoffs and the bond issue have been implemented. It is also not known as of this writing whether there has been a successful sale of the A. Holly Patterson Nursing Home beds.

Although the County has guaranteed the bonds, the fact that there is no acceleration upon default by the Medical Center, places the County in no worse position than it would have been and that coupled with the mortgage on the real estate, it is believed that the County’s position vis a vis the Medical Center has somewhat improved.

No opinions are offered as to whether or not the County would be forced to “step up to the plate” in the event of an impending bankruptcy of the Medical Center (due to political, social or other similar concerns). This is however, a realistic issue and one that the County must always bear in mind as it reviews the Medical Center as a continuing operation.

We have no financial information subsequent to September with respect to the Medical Center although, year end reports will be requested.